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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1944

No. 293

MUTUAL BENEFIT HEALTH & ACCIDENT ASSOCIATION, A CORPORATION,

Petitioner,

vs.

UNITED CASUALTY COMPANY, A CORPORATION; CRAFTSMAN INSURANCE COMPANY, A CORPORATION, AND HAROLD P. LACROIX.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT AND BRIEF IN SUPPORT THEREOF.

PHILIP E. HORAN,
GEORGE J. CLEARY,
V. J. SKUTT,
Counsel for Petitioner.

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Respondents.

PETITION FOR WRIT OF CERTIORARI AND BRIEF IN SUPPORT THEREOF.

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Petitioner, Mutual Benefit Health & Accident Association, a corporation, respectfully shows to this honorable Court:

Statement of the Matters Involved.

This action was originated by the filing of a petition for a declaratory judgment in the United States District Court for the District of Massachusetts at Boston. The plaintiff

(petitioner) is a resident of Nebraska. The defendants (respondents) are residents of the State of Massachusetts. The action was filed on October 30, 1941, under the Federal Declaratory Judgment Statute. (Section 274 (d), Title 28, United States Judicial Code.) Plaintiff prayed for a construction of a reinsurance contract and the solution of a dispute existing thereon between the plaintiff and defendants involving in excess of the jurisdictional sum of $3,000 (R. 11).

Defendant, United Casualty Company, engaged in the health and accident insurance business, entered into a reinsurance agreement with plaintiff, Mutual Benefit Health & Accident Association, also engaged in that business, the effective date of which was July 1, 1940. The subject matter of the agreement was the hospital expense policies of the United Casualty. A few days thereafter defendant, United Casualty, consummated an agreement with defendant, Craftsman Insurance Company, also engaged in the health and accident insurance business, in which agreement, United Casualty transferred to the Craftsman all of its assets and remaining business. Thereby Craftsman Insurance Company assumed all liabilities of United Casualty. The reinsurance treaty, which is the basis of plaintiff's petition for Declaratory Judgment, is found at pages 17, 18 and 19 of the Transcript of Record. The portions material to this petition are as follows:

> This Agreement is made and entered into by and between Mutual Benefit Health and Accident Association of Omaha, Nebraska, hereinafter called the "Association", and United Casualty Company, of Westfield, Massachusetts, hereinafter called the "Company".
>
> "The subject matter of this contract is the Hospital Expense Insurance business of the Company consist-

ing of Hospital Expense Indemnity policies and Surgical Operation or Physician Fee riders attached thereto issued by the Company and in force July 1, 1940.

"The Company has heretofore, among other things, been engaged in the Hospital Expense Insurance business and has outstanding a large number of Hospital Expense Indemnity policies some of which provide by rider benefits for physicians' and surgeons' fees, and this business is hereinafter referred to as 'Hospital Insurance'. * * *

"It is the desire and intention of the Company to pay to the Association cash to cover one hundred (100%) per cent gross unearned premium reserve on these policies in force July 1, 1940, *plus cash in an amount sufficient to constitute an adequate reserve to adjust and pay all claims under such policies incurred prior to July 1, 1940, and unpaid by the Company on that date.* * * *

"All such claims paid by the Association's auditor shall be paid by draft upon the Association. The amount of any claim paid by the Association's auditor, if the claim was incurred prior to July 1, 1940, shall be considered the amount of actual reserve on that claim as of July 1, 1940. In ascertaining whether claims were incurred prior to July 1, 1940, *each claim will be considered on its merits and will be taken to have been incurred prior to July 1, 1940, if the insured's accident occurred prior to that date or if his sickness first became apparent prior to that date. In the event of any disagreement between the Company and the Association's auditor with respect to the incurred date of any claim, the Insurance Department's Examiner shall resolve the doubt.* * * *" (R. 17 and 18.) (Italics ours.)

It is admitted that plaintiff paid all claims under said reinsured policies, including the claims on which the "incurred date" was prior to July 1, 1940. Although the unearned premiums paid to plaintiff by defendant, United

Casualty, covered the period subsequent to July 1, 1940, only, United Casualty and co-defendant Craftsman refused to reimburse the plaintiff, or to arrive at the actual reserve, for the amount actually paid by plaintiff for certain claims on which the incurred date was prior to July 1, 1940. The basis for this refusal is set out in the joint answer of defendants, United Casualty Company and Craftsman Insurance Company, as "all disputes between the plaintiff and United Casualty Company involving the construction of their contract have been previously resolved by the examiner from the Insurance Department of the Commonwealth of Massachusetts, who was specifically designated by the parties in the contract as the one to resolve the very dispute and controversy sought by the plaintiff to be submitted to the Court for decision in this proceeding" (R. 21).

After the defendants had filed their answer containing that allegation, the plaintiff filed a motion to join as defendant the "Examiner from the Insurance Department of the Commonwealth of Massachusetts" referred to in defendant's answer. The motion was granted (R. 29-30). Defendant Examiner LaCroix thereafter filed an answer in this case in which he alleged,

> "That in determining the amount of the claim reserve to be paid by the defendant United Casualty Company to the plaintiff, *the defendant LaCroix determined the incurred date in all so-called maternity cases as the date of hospitalization of the insured, that is, the date when said insured entered the hospital, and if such entry into a hospital was not on or prior to July 1, 1940, determined that the claim made for hospitalization should not be set up or allowed as a claim incurred prior to July 1, 1940, and has taken all maternity cases as a whole and has ruled and resolved that in all said maternity cases where the insured was not in the hospital on or prior to July 1, 1940, liability therefor was placed by said contract upon the petitioner herein*" (R. 32). (Italics ours.)

The case was never tried on its merits. The District Court dismissed plaintiff's petition on the ground that the plaintiff could not "by a suit for a Declaratory Judgment reopen the questions which it referred to a neutral for a binding decision, and which the neutral decided against the plaintiff" (R. 49). Since the answer of "the neutral" alleged that he had not followed the terms of submission of the agreement, i. e., "*each claim* will be considered on its merits and will be taken to have been incurred prior to July 1, 1940, if the insured's accident occurred prior to that date or if his sickness first became apparent prior to that date." (Italics ours.) (Reinsurance Agreement, 2nd paragraph, R. 19), but on the contrary that he had "*taken all maternity cases as a whole* and has ruled and resolved that in all said maternity cases where the insured was not in the hospital on or prior to July 1, 1940, liability therefor was placed by said contract on petitioner herein" (italics ours) (Paragraph numbered 4 of Answer of Examiner LaCroix, R. 32), the plaintiff continued to seek a review of the "neutral's" findings and appealed. The Circuit Court of Appeals for the First Circuit affirmed the ruling of the District Court as quoted (R. 49). From this holding of the First Circuit Court of Appeals, this Petition for Writ of Certiorari is brought.

Jurisdiction.

This Court has jurisdiction to review the judgment under provisions of Section 240 (a) of the United States Judicial Code as amended to become Section 347 (a), Title 28, U. S. Code.

Questions Presented.

1. Where a reinsurance agreement provides for the assumption of liability on the part of one party for claims,

the incurred date of which claims precedes the effective date of the agreement, and where the agreement further provides for an "adequate reserve" when the full liabilities become known, is a provision in said agreement appointing a "neutral" to resolve disputed claims in accordance with a formula laid down in the reinsurance agreement a bar to a petition for declaratory judgment to resolve a dispute created by the failure of a neutral to act pursuant to said formula, and to establish said "adequate reserve"?

2. Under the provisions of the Federal Declaratory Judgment Act, can a trial judge, having taken jurisdiction, refuse to review the action of the parties and the "neutral" which produced the controversy upon the ground that the appointment of said "neutral" to decide certain disputes in accordance with certain formula renders such a review improper where the answer of the "neutral" filed to the petition for Declaratory Judgment admits that he failed to follow the formula laid down in the agreement which created him?

3. Where the Supreme Court of the state where the contract was executed has repeatedly held that the appointment of an arbitrator, referee or "neutral" is not a bar to an appeal from his findings nor a judicial review thereof where said arbitrator, referee or "neutral" did not follow the formula or terms of submission in making his award (*Palmer* v. *Clark*, 106 Mass. 373; *Estes* v. *Mansfield*, 6 Allen 69; *Boston Water Power Co.* v. *Gray*, 6 Met. 131, 167) is such a rule of the State Court binding on a Federal Court called upon in a Federal Declaratory Judgment proceedings to construe said contract?

Reasons Relied On for the Allowance of the Writ.

1. The decision of the Court of Appeals is contrary to and in direct conflict with the law of the State of Massachusetts as determined by

Boston Water Power Co. v. *Gray*, 6 Met. 131;
Cavanaugh v. *Dooley*, 6 Allen 66;
Estes v. *Mansfield*, 6 Allen 69;
Rowe v. *Williams*, 97 Mass. 163;
Palmer v. *Clark*, 106 Mass. 373;
Wood v. *Humphrey*, 114 Mass. 185;
Pearl v. *Harris*, 121 Mass. 390;
Emerson v. *Wadman*, 122 Mass. 384;
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White v. *Middlesex R. R. Co.*, 135 Mass. 216;
Miles v. *Schmidt*, 168 Mass. 339;
Doherty v. *Phoenix Ins. Co.*, 224 Mass. 310;
Patton v. *Babson Statistical Corp.*, 259 Mass. 424;
Fitzgerald Co. v. *Southbridge Etc. Co.*, 304 Mass. 130;
Lakube v. *Cohen*, 304 Mass. 156;
B. Fernandez & Hnos, S En C., v. *Rickert Rice Mills, Inc.*, 119 Fed. (2d) 809 (First Circuit).

2. The decision of the Court of Appeals is in conflict with the Constitution of the United States, the prior decisions of the First Circuit Court of Appeals, and the following decisions of the Supreme Court.

Erie Railroad Co. v. *Tompkins*, 304 U. S. 64, 58 S. Ct. 817, 82 L. Ed. 1188;
Ruhlin v. *New York Life Ins. Co.*, 304 U. S. 202, 58 S. Ct. Rep. 860, 82 L. Ed. 1290;
Rosenthal v. *New York Life Ins. Co.*, 304 U. S. 263, 58 S. Ct. 874, 82 L. Ed. 1330;
Gammino v. *Town of Dedham*, 164 Fed. 593 (First Circuit);

B. Fernandez & Hnos, S En C., v. *Rickert Rice Mills, Inc.*, 119 Fed. (2d) 809 (First Circuit).

3. The Court of Appeals erred in holding that where the District Court had taken jurisdiction in a Federal Declaratory Judgment proceedings, it could refuse to review a justiciable controversy where no action was pending in any other Court and where in similar actions this Court has held that the Federal Declaratory Judgment Act was applicable. The action of the District Court in dismissing the petition was an abuse of discretion.

Borchard on Declaratory Judgments, 2nd Ed., pp. 313-4;

Brillhart v. *Excess Ins. Co.*, 316 U. S. 491; 62 S. Ct. 1173; 86 L. Ed. 1620;

Employers Liability Assur. Corp. v. *Ryan*, 109 Fed. (2nd) 690; 311 U. S. 722, 85 L. Ed. 470, 60 S. Ct. 1107;

Maryland Casualty Co. v. *Pacific Coal & Oil Co.*, 312 U. S. 270, 61 S. Ct. 510, 85 L. Ed. 826, 1 Fed. Rules Dec. 295.

Prayer for Writ.

Wherefore, your petitioner respectfully prays that a Writ of Certiorari be issued by this Honorable Court and that the judgment of the First Circuit Court of Appeals may be reversed.

PHILIP E. HORAN,
GEORGE J. CLEARY,
V. J. SKUTT,
Counsel for Petitioner.

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Respondents.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

I.

Prior Opinion Herein.

The judgments of the Trial Court are found at pages 33 and 35 of the Record. The memorandum opinion of the Trial Court is found at pages 36 to 38 of the Record. The opinion of the Court of Appeals appears at pages 44 to 51 of the Record. It is reported at 142 Fed. (2d) 390.

II.

Jurisdiction.

1. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925, becoming Section 347 (2), Title 28, U. S. Code.

2. Date of the judgment in the Trial Court is June 11, 1943 (R. 35). An appeal was duly perfected to the Circuit Court of Appeals for the First Circuit and the opinion of that Court is dated April 21, 1944 (R. 44).

3. A stay of mandate until further order of the Court was entered on the 5th day of May, A. D. 1944 (R. 52).

4. An order extending time within which to file Petition for writ of Certiorari to and including August 17, 1944, was signed by Mr. Justice Rutledge on July 3, 1944 (R. 52).

III.

Statement of Case.

We supplement, as concisely as possible, the statement of issues as set forth in the Petition for Writ.

United Casualty Company was losing money on its hospital expense policies and ceded all of that type of insurance to the plaintiff, effective July 1, 1940. At that time it paid to the plaintiff full unearned premiums on policies still in force on July 1, 1940 (R. 17). For example, if the premium on a policy had been paid on January 1, 1940 to cover a year's premium, the United Casualty paid one-half of that amount to the plaintiff which would cover the remaining period for which the premium was paid, from July 1, 1940. But the United Casualty Company retained all of the premium covering that portion of the time prior to July 1, 1940. On the effective date of the reinsurance contract there were many policy-

holders with claims pending and unpaid, and others who had claims incurred (having become sick or hurt), but who had not yet reported their claims. Plaintiff agreed in the reinsurance contract to pay all policy claims (R. 17). The payment of claims incurred after July 1, 1940 was the plaintiff's own responsibility as it had received the premium to cover the risk after July 1, 1940. This was the unearned premium as of that date. But the payment of claims incurred prior to July 1, 1940, was also a liability assumed by the plaintiff insofar as the policyholders were concerned. So the United Casualty Company in the agreement promised to pay plaintiff an "adequate reserve" to cover "all claims" (R. 17). The amount actually paid on such a claim was to be the actual reserve on that claim (R. 19). If the policyholder had become sick or hurt prior to July 1, 1940, the claim was to be taken as having been incurred before July 1, 1940, even though the hospital confinement did not occur until after that date (R. 19). That is very clear in the agreement. *The reinsured policies provided that claims were payable upon proof of loss. The proofs of loss always showed the date of hospital confinement. There never was and never could be any dispute about that date. But in the proofs of loss facts were elicited from which the date the accident occurred or the sickness became apparent (in all cases, including pregnancy) could be ascertained as to each claim that was paid. It is common knowledge that opinions may differ about when or on what date a given illness first originates or becomes apparent. The claimant and the attending physician sometimes give different versions in the proofs of loss. That is when the questions or disputes as to incurred dates would arise.* If there were a dispute as to the incurred date, i.e., the date on which the policyholder first became sick or hurt, *each claim* was to be considered on its merits, and the Insurance Department Examiner

was to settle the controversy thereon between the United Casualty Company and the plaintiff. A formula for resolving the dispute was laid down in the reinsurance treaty (R. 19).

The Examiner did settle all disputes according to the formula except for approximately 1050 claims. It happens that all of these were claims for hospitalization on account of pregnancy. As a matter of fact, and as a matter of record (see the answer of the Insurance Department Examiner, page 32 of the Record) he refused to follow the formula and to consider "each claim" on its merits. He did not determine the incurred date by the date the sickness first became apparent. He substituted his own rule and said that the incurred date was the date of entry into the hospital (R. 32).

A reinsurance treaty is involved. The reinsurer (plaintiff) did not buy the business. It was paid to take over the business and assume the liability. The payment was to cover the liabilities assumed by the reinsurer (an "adequate reserve"). No margin for profit was included, but the reserve to cover unearned premiums and incurred claims was to be "adequate" for the purposes of the reinsurance agreement. The agreement so stipulated (R. 17). After the execution of the agreement the United Casualty Company transferred its remaining or other health and accident business, and all of its assets, to the Craftsman Insurance Company. But the "adequate reserve" promised plaintiff under the reinsurance agreement was to constitute a lien until reimbursement to plaintiff for the payment of "all claims" where the incurred date was prior to July 1, 1940 (R. 18). The reason for this was that the plaintiff had not received any premium or unearned premium to cover any period of coverage or risk prior to July 1, 1940. Such premiums had been previously remitted by the policyholders to the defendant United Casualty Com-

pany and have been retained in their entirety for the period prior to July 1, 1940 by said company or its successor defendant Craftsman, at all times unto this date.

IV.

Specification of Errors.

The Court of Appeals for the First Circuit erred in that

1. It held that a Declaratory Judgment proceedings would not lie to determine a dispute involving an "adequate reserve" under an agreement providing for such reserve, where the parties disagreed and where a neutral appointed by the agreement admits that he did not follow its formula for determining the dispute.

2. It held that the actions of a "neutral" were not judicially reviewable where said acts failed to follow the terms of submission which he was bound to follow under the law of the state wherein the agreement was executed.

3. It held that an arbitrator or referee created by an agreement to perform certain duties under a formula laid down in said agreement who admits in his answer to a petition for a Declaratory Judgment review, that he did not follow such formula, is clothed, as a matter of law, with such power and authority that his acts were binding upon the parties and not subject to judicial review.

V.

Summary of Argument.

POINT A.

(Specification 1)

The terms of the reinsurance treaty whereby the plaintiff was liable for claims unpaid on July 1, 1940, the date of the agreement, when the incurred date of such claims

was prior to that date, coupled with the provision of the reinsurance treaty calling for an "adequate reserve" to be paid to plaintiff, and a formula for fixing the same, required the "neutral" to calculate the "adequate reserve" in accordance with said formula. His failure to do so required a judicial review of his acts and a determination of the dispute. A petition for Declaratory Judgment was the means provided by law to obtain such a judicial review and determination. It was error for the Court to deny it.

POINT B.

(Specification 2)

The law of Massachusetts where the contract was executed required a "referee" or "arbitrator" or "neutral" to follow the terms of submission of the agreement which created him. The District Court and the Court of Appeals should have applied the law of Massachusetts.

POINT C.

(Specification 3.)

The answer of the "neutral" (R. 32) in which he alleges in effect that he "took all maternity cases as a whole and ruled that the incurred date on all such cases where hospitalization did not occur prior to July 1, 1940 was the date of entry into the hospital" was contrary to the condition of submission. This allegation required the District Court to review his acts with a view of determining whether or not in taking such action he had complied with the formula or terms of submission contained in the reinsurance agreement, to-wit: "Each claim will be considered on its merits and will be taken to have been incurred prior to July 1, 1940, if the insured's accident occurred prior to that date or if his sickness first became apparent prior to that date." The

action taken by the "neutral" as alleged in his answer constituted a violation of that portion of the formula which required him to take "each claim on its merits" and to fix the incurred date as the date the sickness became apparent.

VI.

ARGUMENT.

Point A.

(Specification 1.)

The parties, being unable to agree on an "adequate reserve" under the terms of the reinsurance agreement, were involved in a controversy within the meaning of the Federal Declaratory Judgment Act. (Act. of June 14, 1934, 48 Statutes at Large 955, Chapt. 512, Judicial Code. Paragraph 274(d) 28 U. S. C. A. paragraph 400.) The fact that the agreement referred such disputes to an arbitrator or neutral did not solve this controversy nor eliminate it. The neutral by his own pleadings found on page 32 of the Record had not followed the condition of submission. Therefore, his acts, or rather his failure to act, constituted a nullity. The position of the parties, so far as the existence of a justiciable controversy was concerned, remained the same as if no provision for an arbitrator or neutral had been contained in the agreement.

Mr. Chief Justice Hughes in *Aetna Life Insurance Company* v. *Haworth*, 300 U. S. 227, 57 Sup. Ct. Rep. 461, 81 L. Ed. 617, 108 A. L. R. 1000, said:

> "Where there is such a concrete case admitting of an immediate and definitive determination of the legal rights of the parties in an adversary proceeding upon the facts alleged, the judicial function may be appropriately exercised although the adjudication of the

> rights of the litigant may not require the award of process or the payment of damages." 81 L. Ed. 622, 300 U. S. 241-43.

Further in the opinion of this case the same Court said,

> "The Declaratory Judgment Act of 1934, in its limitation to 'cases of actual controversy', manifestly has regard to the constitutional provision and is operative only in respect to controversies which are such in a constitutional sense. The word 'actual' is one of emphasis rather than of definition. Thus the operation of the Declaratory Judgment Act is procedural only. In providing remedies and defining procedure in relation to cases and controversies in the constitutional sense, the Congress is acting within its delegated power over the jurisdiction of the Federal Courts which the Congress is authorized to establish. Exercising this control of practice and procedure the Congress is not confined to traditional forms or traditional remedies. In dealing with methods within its sphere of remedial action the Congress may create and improve as well as abolish or restrict. The Declaratory Judgment Act must be deemed to fall within this ambit of congressional power, so far as it authorizes relief which is consonant with the exercise of the judicial function in the determination of controversies to which under the Constitution the judicial power extends." 300 U. S. 239-41, 81 L. Ed. 621.

Following the construction of the Declaratory Judgment Act in the *Aetna Life* case, *Supra*, this Court held in *Maryland Casualty Company* v. *Pacific Coal & Oil Company*, 312 U. S. 270, 61 Sup. Ct. Rep. 510, 85 L. Ed. 826 that where an actual controversy exists, and the other jurisdictional requirements are found, an action for review by Declaratory Judgment will lie. And in *Brillhart* v. *Excess Insurance Company of America*, 121 F. (2d) 776, the Circuit Court of Appeals for the Tenth Circuit reversed a holding by the District Court dismissing a petition for Declaratory

Judgment involving a reinsurance agreement. The majority opinion of this Court reversed the holding of the Court of Appeals because of the effect of a proceedings pending in the State Court. (Same case, 316 U. S. 491, 86 L. Ed. 1620, 62 Sup. Ct. Rep. 1173.) There are no State Court proceedings pending in the instant case. And there can be no question under the holdings of the national Courts, since the enactment of the Federal Declaratory Judgment Act, that the existence of a controversy in the case at Bar, with the existence of other jurisdictional elements, entitled plaintiff to a review under that Act. Further, that it was an abuse of discretion to refuse it. (*New York Life Ins. Co.* v. *Roe*, 102 Fed. (2d) 28, 123 A. L. R. 285.)

POINT B.

(Specification 2.)

Since the holding of this Court in *Erie R. R. Co.* v. *Tompkins*, 304 U. S. 64, 58 S. Ct. 817, 82 L. Ed. 1188 it is mandatory that the United States District Courts and the United States Courts of Appeal follow the judicial law as well as the statutory law of the State, applicable.

The Massachusetts law required a judicial review of the "neutrals" acts. Over one hundred years ago the Massachusetts Supreme Court in *Boston Water Power Co.* v. *Gray*, 6 Met. 131, held that only where not restricted by the terms of submission an arbitrator has authority to decide questions of law and questions of fact as he sees fit, and the parties are bound by his findings. Briefly, in that case, during the course of a trial involving water rights under a contract providing for arbitration between the parties to a written agreement, plaintiff's counsel objected to the admission of any evidence to prove error in the award, on the ground that no error was admitted by the referees and that

it was not competent for the defendant to show by extrinsic evidence any error which they did not admit, and they contended that all the objections taken by the defendant excepting such as were founded on a supposed departure of the award from the submission were objections which could not be maintained unless by the aid of extrinsic evidence, and that the award did not vary from the submission. In discussing the rule on the review of the findings of an arbitrator on a submission or award, Chief Justice Shaw said:

> "It is amongst the rudiments of the law that a party cannot, when a judgment is relied on in support of the bar in action, avoid the effect of it by proving even if he could prove to perfect demonstration that there was a mistake of the facts or of the law. But this *general rule is to be taken with some exceptions or limitations arising either from the submission or from the award, itself,* or from matters distinct from either". (6 Met. at p. 166). (Italics ours.)

In a lengthy opinion the Court discusses the many exceptions to this rule and dwells upon the conditions of submission, saying:

> "Another ground for setting aside the award is a mistake of fact apparent upon the award itself." (6 Met. at p. 168.)

In *Estes* v. *Mansfield,* 6 Allen, 69, an action had been brought upon a promissory note signed by the plaintiff payable to one Charles Estes and endorsed to the plaintiff. After the commencement of the action the parties had submitted the case to arbitrators with a provision that their award should be in accordance with the law and evidence presented. The arbitrators' award was discussed by Chief Justice Bigelow in the opinion as follows:

> "The award is not a bar to the maintenance of this action. The authority of the arbitrators was expressly

limited by the terms of the submission to the making of an award 'in accordance with the law'. This, very clearly, they have not done. They have wholly omitted to pass on the essential fact in issue—whether the plaintiff was a bona fide holder of the note declared on for value before its maturity—on which the right of the defendant to resist payment of the note in the hands of the plaintiff entirely depended. Instead of finding this fact, they seemed to have assumed its existence; and in lieu of making a proper application of the rule of law to such fact, if proved, by making an award in favor of the plaintiff for the amount of note with interest, they have made an award in favor of the defendant leaving the plaintiff to seek a remedy, if any he has, against his endorser for transferring to him a note against which the promissor might have had a valid defense in a suit brought by the payee. This was manifestly a gross mistake of law which led the arbitrator to decide the case on a false issue. On well-settled principles the award is void. Boston Water Power Co. *vs.* Gray, 6 Met. 131, 167" (6 Allen, at p. 70).

This right of review of the findings of an arbitrator or neutral who has failed to follow the condition of submission or formula laid down in the agreement that created him has been adhered to by the Massachusetts State Courts down to the present date. In discussing the rule, the Massachusetts Supreme Judicial Court in *Fitzgerald Construction Co.* v. *Southbridge Etc. Co.* 304 Mass. 130, decided October 25, 1939, stated

"If the parties of their own accord and outside of Court saw fit to submit to arbitration, *without restriction or condition,* the whole matter in dispute, *including all questions* of *law and fact,* then the decision of the arbitrators upon the subject matter in the absence of fraud is binding and conclusive upon the parties, even though the arbitrators may have committed an error of law in reaching their conclusion" (304 Mass. at p. 134). (Italics ours.)

So in *Marsch* v. *Southern New England R. R. Corp.*, 230 Mass. 483, the Massachusetts Supreme Judicial Court repeated the rule as:

> "The general rule undoubtedly is that, *unless restricted by the agreement of submission,* arbitrators are the final judges of both law and fact and an award will not be reviewed or set aside for mistake in either." (2 R. C. L. p. 392, par. 36.)

And in *Doherty* v. *Phoenix Insurance Company,* 224 Mass. 310 the Court points out:

> "The referees were unhampered by any restrictions or conditions" (p. 315, 224 Mass. Rep.).

In another recent decision of the Massachusetts Supreme Judicial Court where the findings of the referee or arbitrator were set aside, we find the Court stating the Massachusetts rule to be:

> "That an agreement between an employer and employee that submission to arbitration of any controversy, claim or demand should be a condition precedent to a resort to an action at law or suit in equity, made the submission a condition precedent to a resort to the Courts, but not to the existence of a substantive cause of action." (*Lakube* v. *Cohen,* 304 Mass. 156.)

In *Patton* v. *Babson Statistical Corp.,* 259 Mass. 424 the same Court was called upon to construe the following provision in a contract:

> "If any question arises as to the interpretation or application of any feature of the plan, the decision of the President shall be final."

The Massachusetts Supreme Judicial Court held that this provision in the agreement did not prevent a Court from reviewing the agreement and holding that the clause quoted did not bar a recovery contrary to the decision appealed from.

First Circuit Court of Appeals Formerly Followed the Rule!

The Court of Appeals for the First Circuit, as late as May 8, 1941, followed the Massachusetts rule. In the case of *B. Fernandez & Hnos, S En C.*, v. *Rickert Rice Mills, Inc.*, 119 Fed. (2d) 809, the First Circuit Court of Appeals said:

> "It is now well settled that the question of the construction of a contract to determine what questions the parties thereto agreed to submit to arbitration is one for the court to decide and not for the arbitrators. (* * * the court here cites numerous authorities).
>
> "To allow the arbitrators conclusively to decide what questions were submitted to arbitration is to allow them finally to determine the extent of their own jurisdiction. If the parties intended that the arbitrators should have the power finally to decide what was to be submitted to them, there is no objection to their doing so, but the courts do not readily *infer* such an agreement." (Italics ours.) (119 Fed. (2d) at p. 814.)

The following appears in the Syllabus of said case:

> "1. The construction of a sales contract to determine what questions the parties thereto agreed to submit to arbitration is one for the Court to decide and not for the arbitrator.
>
> "2. Where there is a conflict between a clause of contract providing for arbitration and one providing for a conclusive certificate, it is the duty of the Court to attempt to reconcile both clauses.
>
> "3. Contract providing for arbitration will be carefully construed in order not to force a party to submit to arbitration a question which he did not intend to be submitted.
>
> "4. A party is never required to submit to arbitration any question which he has not agreed so to submit." (119 Fed. (2d) 809, syllabus).

Even prior to *Erie R. R.* v. *Tompkins, supra,* the First Circuit Court of Appeals in construing a Massachusetts

contract held that an appeal would lie upon the findings of an arbitrator who had failed to follow the rules of submission. (*Gammino* v. *Inhabitants of the Town of Dedham*, 164 Fed. 593.) We shall discuss this case under our argument on Specification #3.

POINT C.

(Specification 3.)

With respect to this specification, we respectfully solicit the Court's consideration of the following decision by the United States Circuit Court of Appeals for the First Circuit: It is *Gammino* v. *Inhabitants of the Town of Dedham*, 164 Fed. 593. Here a contract had been made for the construction of a sewer in the Town of Dedham, Massachusetts, and contained the following provisions:

> "In case of any dispute arising the engineer shall have the right to settle the same, and he shall have the right to determine and interpret the meaning of these specifications and contract to be made under them, and all decisions of the engineer shall be final." (164 Fed. at p. 600). (Note the broad authority conferred upon the arbitrator.)

An important provision of the contract read:

> "The above quantities are not guaranteed, and the commissioners reserve the right to increase or diminish the same within 25%. Upon the quantities above given bids will be compared. These quantities will be a part of any contract made for the prosecution of this work, and when referred to in such contract, include each and every part of the same." (164 Fed. at p. 594.) (The "adequate reserve" for "all claims" clause in reinsurance agreement involved here)

In ruling on this case the Court said:

> "We are of the opinion that, upon a construction of the contract which gives due effect to this provision, the

prices named are to prevail only to the extent of the quantities named, with a 25 per cent margin of variation. The contract fails to fix a price for quantities in excess of this. * * * The limitation to a 25% variation was inserted for a purpose. Except for this provision, the prices named would prevail for all the work done, even if it should turn out that the actual portion of earth and rock excavation were substantially different from what was contemplated. An attempt to hold a contractor strictly to the prices named for an amount of work substantially different from what was contemplated might result in hardship so great as to show mutual mistake concerning the subject matter of the contract and thus endanger the entire contract. * * * The auditor found that the sum total of earth and rock excavation did not exceed by 25% the sum total of the number of cubic yards stated in the estimate for earth and rock excavation, and, therefore, that the prices named in the contract applied to all rock excavation. Counsel for defendant in error contends that this is in accordance with the proper construction of the contract. We are of the opinion that this is erroneous and that it not only violates the terms of the contract, but leads to an unreasonable result" (164 Fed. at pp. 594, 595).

The allegation contained in the answer of the Insurance Department Examiner, stating that he "has taken all maternity cases as a whole" (R. 32) when it was provided in the reinsurance agreement that "each claim will be considered on its merits" (R. 19) constitutes a conclusive and uncontraverted showing in the record of this case that the arbitrator violated the condition of submission contained in the agreement. His additional allegation, "That in determining the amount of the claim reserve to be paid by the defendant United Casualty Company to the plaintiff, the defendant LaCroix determined the incurred date in all so-called maternity cases as the date of hospitalization of the insured, that is, the date when said insured entered the

hospital" (R. 32) in the face of the provision in the reinsurance agreement reading "each claim * * * will be taken to have been incurred prior to July 1, 1940 if the insured's * * * sickness first became apparent prior to that date" (R. 19), is a further, conclusive, and uncontroverted showing in the record of this case that the arbitrator did not follow the condition of submission contained in the agreement.

But the District Court and the Circuit Court of Appeals, in their opinions in this case, *infer* from the language of this reinsurance agreement, authority on the part of the arbitrator to set up his own formula in determining the incurred date of maternity or pregnancy claims. We use the word "infer" advisedly. There is nothing in the reinsurance agreement excluding any certain type of claim from the application of the formula. There is no exception contained in the agreement as to maternity or pregnancy claims.

However, the Circuit Court of Appeals in its opinion seems to agree with the arbitrator that a maternity or pregnancy claim is not a sickness claim within the meaning of the reinsurance agreement. "We may say that we are far from convinced that the arbitrator made any mistake in interpreting the contract. The word 'sickness' certainly does not necessarily include 'pregnancy'" (R. 50), 142 Fed. (2d) 394. In this connection we most emphatically and respectfully submit to this Court that where the reinsurance agreement involved uses the language "plus cash in an amount sufficient to constitute an *adequate reserve* to adjust and pay *all claims* under such policies incurred prior to July 1, 1940," (R. 17) and *"all such claims"* (R. 19) and *"each claim"* (R. 19) (italics ours) there can be no doubt whatsoever about the intention of the parties. They were talking about "all the claims" and "each claim." If it had been their intention to exclude any type of claim,

that intention would have been displayed in the contract by saying "except maternity or pregnancy claims." *The exclusion can not be inferred. Neither can it be inferred that the parties intended that the arbitrator set up a new condition of submission or formula for any certain type of claim, pregnancy or otherwise.* In the latest expression from this very Circuit Court of Appeals in *B. Fernandez & Hnos, S En C.*, v. *Rickert Rice Mills, Inc.*, 119 Fed. (2d) 809 (First Circuit), the Court said, "if the parties intended that the arbitrator should have the power finally to decide what was to be submitted to them, there is no objection to their doing so, but the Courts do not readily *infer* such an agreement" (italics ours). (119 Fed. (2d) 814.) In so holding the Court of Appeals for the First Circuit was following the Massachusetts Law as determined by decisions of Massachusetts State Courts for generations.

The Circuit Court of Appeals dismisses the suggestion that the Massachusetts statutes under which the policies involved were approved did not recognize "pregnancy or maternity" insurance coverage as such (R. 52). (142 Fed. (2d) 394.) The fact is, and we repeat it here, and quote the statute in the appendix hereof, the policies could only provide coverage for sickness or accidental injury under the Massachusetts law. The term "sickness," as used in the policies (insuring clause etc.), in the statutes *and in the reinsurance agreement* was an all inclusive term. It includes, in addition to diseases, benign tumors, pregnancies, normal or abnormal growths or any other condition causing hospitalization. The claims for benefits and the checks in payment thereof were under the sickness branch of insurance coverage. Anyway the prospective mothers felt they were sick and filed claims. The plaintiff paid—although defendants had received and retained the premiums covering the time the sickness began. The defend-

ants have not challenged the propriety of the payment to policyholders by plaintiff. They owe the plaintiff therefor under the agreement.

The Circuit Court of Appeals further rests its decision of affirmance upon a stipulation signed by one of plaintiff's attorneys and reading in part, "that the arbitrator did not exceed the authority conferred upon him but the plaintiff contends that the examiner misconstrued the provisions of the contract dealing with the incurred date of claims and that an adequate reserve was not set up for pregnancy claims" (R. 50) (142 Fed. 2nd 394). Of course, it is not contended by plaintiff that the arbitrator exceeded his authority when he considered pregnancy claims. He was required by the reinsurance agreement to consider them. He would have violated that agreement had he failed to do so. The fact that he did consider pregnancy claims is alleged in his answer. The fact that defendants urge such consideration and his conclusion as binding upon the plaintiff, shows that maternity claims were included under the terms of the reinsurance agreement, the same as any other sickness claims. There being no reference to maternity claims in the agreement, that was the only possible conclusion. However, any doubt about their inclusion is eliminated by the stipulation referred to. But this stipulation certainly can not be construed to mean that in the consideration of the claims, the arbitrator had followed the formula prescribed for him. Such a construction of the stipulation flys in the face of the pleadings and record in this case; particularly the allegations of the arbitrator himself (R. 32). Obviously the language of the stipulation indicated an intention to agree on the proposition that pregnancy claims were included in the reinsurance agreement (we say, as sickness claims) and that by considering these claims the arbitrator did not exceed his authority.

Finally the Circuit Court of Appeals rests its decision of affirmance upon the statement: "the actual reserve found by the arbitrator turned out to be very near this estimated figure, namely $50,412.96" (R. 51) 142 Fed. 2nd 394-5. In the first place there is nothing in the reinsurance agreement to indicate that the "estimated figure" was to approximate an "adequate reserve" (R. 17). With a volume of premiums paid in advance and with much coverage at risk during the period involved, it was not the intention of the parties that the so called "estimated reserve" have any relation to an "adequate reserve." There was no possible way of determining the number of policyholders who would file claims for a sickness incurred prior to July 1, 1940. The so called "estimated reserve" covered only those who had already given notice but who had not been paid. It had no bearing whatsoever on the "adequate reserve" called for by the reinsurance agreement (R. 17). The plaintiff did not agree to be bound by the "estimated figure" or by any maximum or minimum additional figure or percentage relating thereto. Here again please consider the holding in the *Gammino* case, *supra,* where a 25% variance is discussed. It was only after the reinsurance treaty had been in force and effect for many months that the plaintiff had any idea of the total amount paid on claims, the incurred date of which was prior to the effective date of the contract. *Whatever may be found to be the "adequate reserve" upon application of the formula to "all claims" as agreed upon by the parties, is the amount involved in this lawsuit.* That can not be determined until the formula has been applied to the pregnancy claims as called for by the agreement which referred to "all claims" and "each claim" (R. 17-19). The so called "estimated reserve" of $51,000.00 was the figure selected by the defendant United Casualty Company, based on the claims already reported. The plaintiff did not in-

vestigate it nor accept it or anything relating to it. On the contrary the plaintiff required this provision to be inserted in the agreement: "until the *actual amount* is determined *all assets* of the company shall be subject to a lien to secure the payment of *any difference* that may be found due the Association" (R. 18) (italics ours).

Conclusion.

No one knew or could know the amount or approximate amount of that "difference" until all policy claim liability had been discharged. It is admitted that the plaintiff has fulfilled its obligations to the policyholders and has paid all the claims. It is now entitled to a judicial review of the acts of the arbitrator, to produce a determination of the "adequate reserve." This is only in keeping with the language of the contract and pursuant to the precise purpose and rules of the Federal Declaratory Judgment Act.

Therefore, we most respectfully pray that the petition for writ of certiorari be granted in this case to the First Circuit Court of Appeals.

PHILIP E. HORAN,
GEORGE J. CLEARY,
V. J. SKUTT,
Counsel for Petitioner.

APPENDIX.

Federal Rules of Civil Procedure, Rule 57.

"DECLARATORY JUDGMENTS. The procedure for obtaining a declaratory judgment pursuant to Section 274 (d) of the Judicial Code, as amended, U. S. C., Title 28, Para. 400, shall be in accordance with these rules, and the right to trial by jury may be demanded under the circumstances and in the manner provided in Rules 38 and 39. The existence of another adequate remedy does not preclude a judgment for declaratory relief in cases where it is appropriate. The court may order a speedy hearing of an action for a declaratory judgment and may advance it on the calendar."

Massachusetts General Laws, Chapter 175, Section 47.

"Purposes of incorporation. Kinds of business. Companies may be incorporated under and subject to the provisions of this chapter for the following purposes: Sixth, * * * (d) to make insurance upon the health of individuals; or (e) to insure the payment of workmen's compensation benefits under chapter one hundred and fifty-two."

Massachusetts General Laws, Chapter 175, Section 108.

"Accident or health policies, approval and contents. No policy of insurance against loss or damage from disease or by the bodily injury or death by accident of the insured shall be issued or delivered in the commonwealth: (a) until a copy of the policy and the table of rates or manual of risks of the company has been on file with the commissioner for at least thirty days, unless before the expiration of said thirty days the commissioner shall have approved the policy in writing; nor (b) if the commissioner notifies the company in writing that in his opinion the form of said policy does not comply with the laws of the commonwealth, specifying the reason for his opinion, provided that such action of the commissioner shall be subject to review by the supreme judicial court; * * *"

AUG 31 1944
CHARLES ELMORE CROPLEY
CLERK

Supreme Court of the United States.

OCTOBER TERM, 1944.

No. 293.

MUTUAL BENEFIT HEALTH & ACCIDENT ASSOCIATION,
Petitioner,

v.

UNITED CASUALTY COMPANY, CRAFTSMAN INSURANCE COMPANY, AND HAROLD P. LaCROIX,
Respondents.

BRIEF OF RESPONDENTS UNITED CASUALTY COMPANY AND CRAFTSMAN INSURANCE COMPANY IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

RALPH E. TIBBETTS,
Attorney for Respondents.

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I.

Prior Opinion.

The judgment of the Trial Court and the memorandum of opinion of that Court are found on pages 33 to 38 of the record, and the opinion of the Court of Appeals, confirming the decision of the Trial Court, appears at pages 44 to 51 of the record and is reported in 142 Fed. (2d) 390.

II.

Jurisdiction.

This case comes here on petition for writ of certiorari to the First Circuit Court of Appeals under the provisions of Section 240 (a) of the Judicial Code as amended, being Section 347 (2), Title 28, United States Code.

III.

Statement of Case.

The petitioner made a written agreement with the United Casualty Company for the taking over of the latter company's hospitalization expense insurance policies, which provided among other things that United Casualty Company should pay "cash" to the petitioner "sufficient to constitute an adequate reserve to adjust and pay all claims" under insurance policies "incurred prior to July 1, 1940," and not previously paid by United Casualty Company (Rec. 17).

The parties agreed that such claim reserve as fairly estimated by them amounted to $51,000 (Rec. 18). The parties agreed further that the "actual amount" of the claim reserve should "be ascertained by the Insurance Department of the Commonwealth of Massachusetts," and, when so ascertained, any necessary adjustments would then be made (Rec. 18).

It was agreed that, if a claim had been "incurred prior to July 1, 1940," and the petitioner paid an amount in settlement of same, the amount so paid should be the reserve on that particular claim. No controversy has at any time existed as to the meaning or application of this clause (Rec. 19, par. 4).

It was further agreed that "in the event of any disagreement between the Company and the Association's auditor

with respect to the incurred date of any claim, the Insurance Department's examiner shall resolve the doubt" (Rec. 19, par. 4). In open court the parties conceded that this provision of the contract should be interpreted to mean that the decision of the examiner should be final and binding on the parties (Rec. 37).

A disagreement arose between the petitioner and United Casualty Company as to whether, when hospitalization in a childbirth case occurred after July 1, 1940, in ascertaining the date when the claim was incurred, the date the pregnancy "first became apparent" should be determinative. The insurance policies themselves covered hospitalization only, and no claim could arise until the hospitalization occurred (Rec. 12). The parties, however, in clause 4 of their contract had agreed to a provision which, in cases to which it applied, would result in a claim being incurred as of a date "sickness first became apparent" rather than the date of hospitalization (Rec. 19).

The parties, not being able to agree that the term "sickness" as used in clause 4 of the contract was intended to be inclusive of the condition of pregnancy so that when pregnancy "first became apparent" the claim was incurred, referred their disagreement as to the incurred date of a maternity case to the insurance examiner to "resolve the doubt."

The examiner decided the term "sickness" as used in the contract did not include pregnancy and that the incurred date of each maternity case as it was presented should be determined by reference to the date of hospitalization. He determined the amount of the actual claim reserve on that basis.

The amount of the actual reserve as determined by the examining representative of the Insurance Department of the Commonwealth of Massachusetts was $50,412.96 (Rec. 27; Court Opinion, Rec. 51) as against the $51,000 the par-

ties estimated in advance and as compared with the sum of approximately $120,000 claimed by the petitioner on its interpretation of the contract term "sickness."

It was stipulated and conceded by the parties, as appears in the memorandum opinion of the Court (Rec. 37), that the examiner "was the proper person to act as arbitrator; he proceeded in good faith; he did not consider topics beyond the authority conferred upon him; he completed his work and made a final report to the parties and his only mistake, if he made one at all was a mistake of law in the construction he gave to the agreement in its application to maternity cases."

IV.

Argument.

The petitioner's contention is that the contract of the parties contained "terms of submission" binding on the arbitrator and with which the arbitrator did not comply; further, that to uphold his decision is therefore contrary to the controlling law of Massachusetts.

It is stipulated that the arbitrator "did not consider topics beyond the authority conferred upon him" (Rec. 37); "that he did not exceed the authority conferred upon him," but the petitioner contended that he "misconstrued the provisions of the contract dealing with the incurred date of claims" (Rec. 39). In other words, the only error of the arbitrator, if any, as conceded by the petitioner, is that in applying the contract, as he was obliged to apply it in the performance of his duties, he made a mistake of law (Rec. 37).

The clauses of submission as set out in the contract are found in paragraphs 1 and 4. Paragraph 1 provides: "As soon as practicable after July 1, 1940, the actual amount of such claim reserve shall be ascertained by the Insurance

Department of the Commonwealth of Massachusetts without expense to either of the parties hereto" (Rec. 18). Paragraph 4 provides: "In the event of any disagreement between the Company and the Association's auditor with respect to the incurred date of any claim, the Insurance Department's examiner shall resolve the doubt" (Rec. 19).

The contract nowhere sets out any limitations on the examiner in resolving a dispute that might arise. When a disagreement developed as to the incurred date of claims in childbirth cases, that part of the arbitration reference set out above and appearing in paragraph 4 of the contract came into operation, and the disagreement was referred to the examiner to resolve the doubt. The determination of this disagreement by the examiner necessitated the construction by him of the clause in the contract dealing with the incurred date of claims in certain specified cases. The examiner interpreted such clause in good faith and applied his interpretation to each maternity case as it subsequently became involved in the determination of the actual claim reserve.

On such a state of facts, the petitioner claims in its "Specification of Errors" that the examiner "admits" he did not follow a "formula" which the petitioner contends was embodied in the "terms of submission." The petitioner gives to the clause in paragraph 4 which binds the parties to a certain rule in ascertaining the incurred date of claims in accident and sickness cases an interpretation which would also include childbirth cases. The petitioner then contends that this clause was a "formula" which the examiner had to follow, subject to the condition that in following it the examiner was required to interpret it in the same way the petitioner interpreted it. There is nothing in the agreement which places such limitation or condition on the examiner when in settling a disagreement he had to construe and apply the clause in paragraph 4.

It is asserted that the examiner in dealing with hospitalization for childbirth cases failed to consider each claim on its merits. There is no contention that the amount payable to the insured on each maternity claim was not separately determined according to the merits of the claim, but the contention is rather that, when the examiner interpreted the word "sickness" not to include pregnancy, there resulted a failure to consider each maternity case on its merits. This in the face of the examiner's statement (Rec. 32, par. 4) that he "determined the incurred date in all so-called maternity cases as the date of hospitalization of the insured, that is, the date when said insured entered the hospital, and if such entry into a hospital was not on or prior to July 1, 1940, determined that the claim made for hospitalization should not be set up or allowed as a claim incurred prior to July 1, 1940."

He goes on to state that, taking maternity cases as a whole, he "has ruled and resolved that in all maternity cases where the insured was not in the hospital on or prior to July 1, 1940, liability therefor was placed by said contract upon the Petitioner herein." He thus stated his decision in resolving the dispute that had arisen between the parties concerning the meaning of their contract involving the "incurred date" of claims, and specified his procedure in applying the rule as so interpreted.

The examiner was not construing a clause that in any way dealt with the extent of his powers as arbitrator, but a clause rather that had to do with the respective rights of the parties under the terms of their contract and within the limitation of the subject-matter submitted to his jurisdiction. The petitioner's contention is in effect that the examiner, when called upon to apply the terms of the contract to the resolving of a disagreement that had arisen, should have interpreted the contract in accordance with the petitioner's interpretation rather than accepting the interpre-

tation of the other parties to the contract. Even if the examiner were in error in interpreting the contract as he did, the petitioner is bound and concluded by the examiner's decision, according to the well-established law of Massachusetts.

Boston Water Power Co. v. *Gray,* 6 Met. 131, at pp. 165, 166 and 167.

Phaneuf v. *Corey,* 190 Mass. 237, at pp. 245 and 247.

2 Ruling Case Law, p. 392, par. 36.

Sturges, Commercial Arbitration (1930 Ed.) p. 296.

It is respectfully submitted that the petition for certiorari should be denied.

RALPH E. TIBBETTS,
Attorney for Respondents.